The ABC's of Low Income Housing Tax Credits

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- What/Who/How much
- Basic Terms
- Basic Requirements
- California’s Goals
- Project Ownership/Project Beneficiaries
- California’s Application process and timelines
- Projects monitoring

Low Income Housing Tax Credits (LIHTC)

- To encourage **private** development of affordable housing
- To Create & Preserve Decent, Safe, Affordable Rental Housing
- Nations most important tool in Affordable Housing Development

LOW INCOME HOUSING TAX CREDIT

- Created by the Tax Reform Act of 1986
  - Section 42 of the Internal Revenue Code
- Governed by the Internal Revenue Service (IRS)
- Administered by State Agencies
- Federal Credits are allocated annually to each state based on population

Qualified Allocation Plan (QAP)

- Each State is required to Have a QAP
- Outlines State Priorities & cites State Regulations
- Outlines Federal Law priorities such as:
  - Projects that target the lowest income
  - Remain affordable the longest
    - Among other priorities…

Tax Credit vs. Tax Deduction

- **Tax Credit** – dollar for dollar reduction in tax liability

- **Tax Deduction** – offset to pre-tax income
- LIHTC projects make use of both types
  - Why some investors will pay more than $1 per tax credit

Basic Requirements

LIHTC Projects Must:

- Be a residential rental property
- Commit to Low Income Occupancy
- Restrict Rents
- Operate as an affordable project for 55 years

Income Restrictions

Minimum Set-A-Sides – Federal Requirement:

- 40% units at 60% of Area Median Income (AMI)

OR

- 20% units at 50% of Area Median Income (AMI)

BUT

- Credits are awarded based on Income restricted units. **(typically 100%)**

Rent Restrictions

Rents are restricted by income group, bedroom size and Area Median Income (AMI)

Example of 2007 rents:

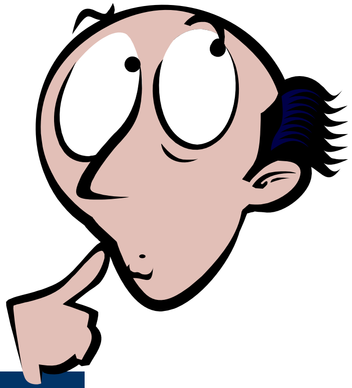
Sacramento County	1 Bdr	4 Bdr
50% AMI	$613	$ 948
60% AMI	$735	$1138

Rent Requirements

- Rents include utility costs and all other costs that are required by owner

Low Income Housing Tax Credits

- **Two Types of Federal Credits:**
  - 70 Percent of eligible costs (**basis**)
    - The **<u>9% Credit</u>**
  - 30 Percent of eligible costs (**basis**)
    - The **<u>4% Credit</u>**
- **Credit Rates:** 7.92% **(9%)** & 3.40% **(4%)**
- **“Lock-in Election”**



WHAT IS BASIS?

- **How Much Credit can you get?**
- You must Determine the **"Eligible Basis"** for your project to figure the amount of tax credits

Determine “Eligible Basis”

- ***<u>Eligible Basis</u>*** is based on the costs of the project
- Includes depreciable assets:
  - Development Costs *minus*:
    - Land, permanent financing, grants, fees, etc.

Determining Basis

- **Qualified Basis**:
  - Qualified Census Tract (QCT) or
  - Difficult to Develop Area (DDA)
  - 130% federal basis boost
- **Adjusted Eligible Basis:** # of low income units (applicable fraction)
  - 100 units total
  - 50 Low income Units = 50% of eligible basis

*****Most projects are 100% Low Income

TCAC - THRESHOLD BASIS LIMITS

- Established by each State
- Determined using actual historical costs
- Dollar limits by # of bedrooms

TCAC Basis Limit Boosts

- **Basis Limit Boosts (increases):**
- **Examples:**

- 20% if project required prevailing wages
- 2% if day care center is part of project
- 10% for Elevator buildings
- 5% distributive energy
    - Will result in a **“Threshold Basis Limit”**

Calculating the Credit Amount

- 9% Tax Credit Example:

- TCAC will use a standard rate of 8.3% for underwriting.

- Apply this to :

Total **<u>Qualified basis</u>**

Calculations of Tax Credits/Equity

Total Development Cost	$8,000,000
Less: Non-eligible (land/soft cost)	1,600,000)
Eligible Basis	$6,400,000
Applicable fraction (% of LIHTC units)	X 100%
Qualified Basis	$6,400,000
Tax Credit Applicable %	X 8.3%
Annual Tax Credit	$ 531,200
Tax Credit Period	X 10 yrs.
	$5,312,000

Calculating the Amount of Credit

	$5,312,000
Equity at $.90 per Credit	X .90
	$4,780,800
Total Development Cost	$8,000,000
Less: Equity	(4,780,800)
Required Debt (gap)	$ 3,219,200

Calculating the Amount of Credit

- Exercise

ANSWERS

• BASIS LIMIT:	$12,807,940
• ELIGIBLE BASIS:	$13,800,000
• ADJ. THRESHOLD BASIS:	$12,807,940
• QUALIFIED BASIS:	$12,807,940
• ANNUAL TAX CREDIT	$ 1,063,059
• 10 YEAR CREDIT:	$10,630,590
• EQUITY @ .95:	$10,099,060
• FUNDING GAP:	$ 4,900,939

Low Income Housing Tax Credit Uses

- 9%: New Construction
  Rehabilitation

- 4%: Acquisition
  New Construction
  Rehabilitation

California's 9% Federal Tax Credit Allocation

- $2.00 Per Capita
- 2008 Estimate: $73 million (9% credits)

9% Federal Tax Credits

- Competitive application process
  - **Threshold and Point system**
- Typically 2 rounds per year
- $2 million application limit
- Credit taken for 10 years
  - $73 million = $730 million

9% Low Income Housing Tax Credits

- Typically, Tax Credits will pay for 50% to 60% of the project costs.
- Other financing could include:
  - Government agency dollars
  - Banks
- Be Aware of some restrictions:

  BMIR financing & Federal Grants

4% Federal Tax Credits

- Non-competitive
- Total available limited by Tax Exempt Bond Authority
- Can apply “Over-the-Counter”
- Credit Taken for 10 years
- 10% Unit @ 50% AMI

Federal Low Income Housing Tax Credit Equity

- Developer sells the right to take credits to investors (for 10 years)
- Price paid reflects: value of the real estate & net present value of the 10 years worth of credits
- From .85 cents to $1.04 per $1 of tax credit (currently trending down)

State Tax Credits

- Available in combination with Federal 9% or 4% Tax Credits
- Credit for 4 years
- Approximately $89 million available (4 year total * not an annual amount)
- **Apply for in the competitive 9% round**

State Policy Priorities
Set-a-Sides & Apportionments

- **Non-Profit set-a-side** **10%**
  - Homeless Assistance Priority
- **Rural set-a-side** **20%**
  - RHS program apportionment
    (14% of the above 20%)

Set-a-Sides & Apportionments

➢ Small Development set-a-side	2%
➢ "At-Risk" set-a-side	5%
➢ Special Needs/SRO set-a-side	2%
➢ Supplemental set-a-side	3%

- ➢ for overages in set-a-sides & geographic regions

Geographic Apportionments

- Los Angeles County 33%
- Central 10%
  - Fresno, Kern, Kings, Madera, San Joaquin, Stanislaus, Tulare
- North & East Bay 10%
  - Alameda, Contra Costa, Marin, Napa, Solano, Sonoma

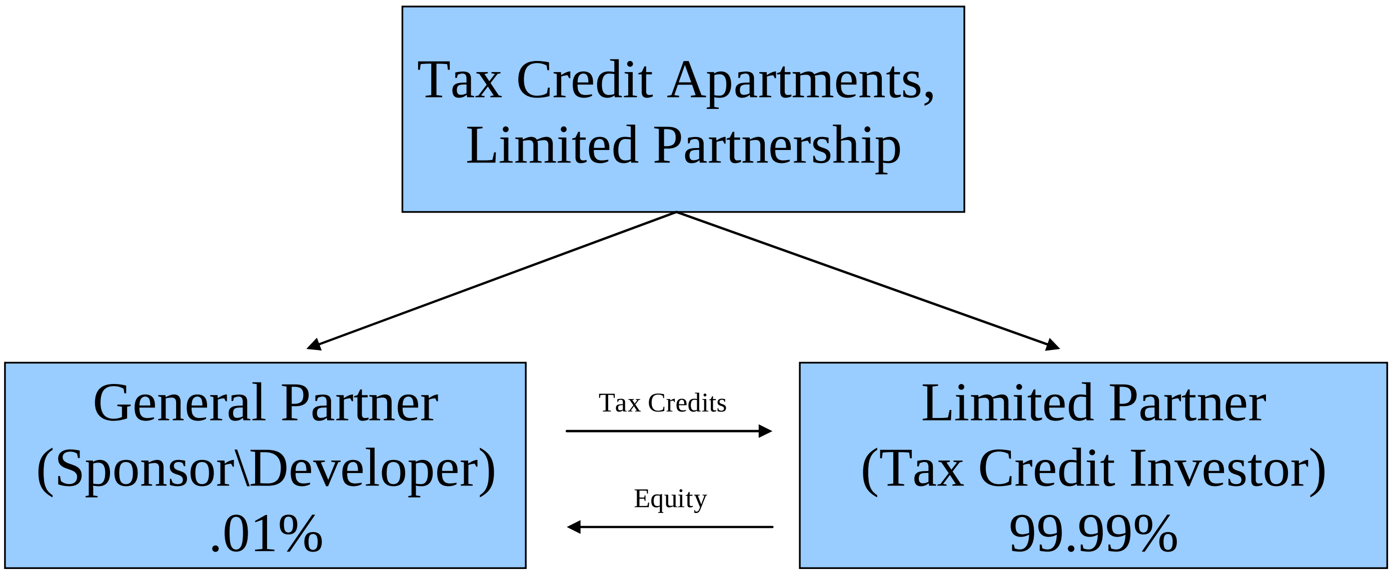
Geographic Apportionments

➢ San Diego County	10%
➢ Inland Empire	8%
➢ San Bernardino, Riverside, Imperial	
➢ Orange County	8%
➢ San Mateo & Santa Clara Co.	6%

Geographic Apportionments

- Capital/Northern Area 6%
  - Butte, El Dorado, Placer, Sacramento, Shasta, Sutter, Yuba, Yolo
- Coastal California 5%
  - Monterey, San Luis Obispo, Santa Barbara, Santa Cruz, Ventura
- San Francisco County 4%

Ownership Structure



Ownership Structure

- Limited Partnership
  - Operating Agreement: Sets Forth Roles, Responsibilities and Compensation
- 0.01% - General Partner / Managing Member
  - Manages Project
- 99.99% - Limited Partner / Investor Member
  - Provides the cash in exchange for Tax Benefits

Tax Credit Syndication

- Syndication Companies match LIHTC projects and Investors
- Accumulate tax credit projects into funds
  - Typically \$50 million to \$300 million
- Structured as Limited Partnerships or Limited Liability Companies

Tax Credit Syndication

- Sell primarily to institutional investors
  - Banks, insurance companies, GSEs (Freddie Mac, Fannie Mae) etc.
- Syndicator conducts partnership negotiations on behalf of the Fund.

Tax Credit Investors

- Investors have a variety of reasons for committing capital.
- Financial incentive: **reduced tax liability**.
- Specific community development goals, regulatory requirements and/or public relations objectives.

Montecito Vista

- Family Housing
- Irvine, CA

Fremont Oak Gardens

Senior Apartments

Plaza Apartments
San Francisco

- Supportive Housing

9% Application & Project Timing

- Application is submitted: April 9 & July 24
- Awards made: June 25 & October 1
- Carry-over Allocation Documents:
  - Due October 31st of Award year
  - Projects not placed-in-service year of award

  taxpayer must incur at least 10% of expected project costs (land and depreciable property).

***Can fix credit rate at this time**

9% Application & Project Timing

- **150 Day Readiness Documents** (scoring):
    - Approximately 5 months after award
- **Final Reservation Documents:**
    - February 1st of the year project will place-in-service
- **Placed-in-Service:**
    - December 31st, 2 years after award

9% Application & Project Timing

- Placed-in-Service Package:
  - Includes 8609 request, etc.
    - 1 year from the last building placed in service date
- Regulatory Agreement is prepared
- 8609 Tax Form request is reviewed & issued

COMPLIANCE MONITORING

- TCAC Staff will monitor within 2 years of project being Placed in Service

- Project will submit annual reports
  - Occupancy
  - Operating Expenses

- TCAC will monitor every 3 years